

**REPORT OF
FINANCIAL EXAMINATION**

**CHARITON COUNTY MUTUAL
INSURANCE COMPANY**

**AS OF
DECEMBER 31, 2003**

**STATE OF MISSOURI
DEPARTMENT OF INSURANCE
JEFFERSON CITY, MISSOURI**

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April 27, 2004
Mendon, Missouri

Honorable Scott B. Lakin, Director
Missouri Department of Insurance
301 West High Street, Room 530
Jefferson City, Missouri 65101

Sir:

In accordance with your examination warrant, a full-scope examination has been made of the records, affairs and financial condition of

CHARITON COUNTY MUTUAL INSURANCE COMPANY

hereinafter referred to as such, or as the "Company". The Company's home office and principal place of business is located at 404 Main Street, Mendon, Missouri, telephone number (660) 272-3322. This examination began on April 26, 2004, and was concluded on April 27, 2004, and is respectfully submitted.

SCOPE OF EXAMINATION

Period Covered

The prior full-scope examination of the Company was made as of December 31, 1998, and was conducted by examiners from the State of Missouri. The current full-scope examination covers the period from January 1, 1999, through December 31, 2003, and was conducted by examiners from the Missouri Department of Insurance.

This examination also included material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

Procedures

This examination was conducted using the guidelines set forth in the Financial Examiners Handbook of the National Association of Insurance Commissioners (NAIC), except where practices, procedures and

applicable regulations of the Missouri Department of Insurance and statutes of the State of Missouri prevailed.

Comments-Previous Examination Report

The comments, recommendations, and notes of the previous examination report dated December 31, 1998, are listed below followed by the Company's response and the current examination findings regarding such comments, recommendations and notes.

History

Comment: The Company was directed to comply with Section 380.271 RSMo. (Guaranty fund required) and obtain a reissued Certificate of Authority with the correct lines (G1, G2 and G3) shown.

Company Response: The Company has obtained a corrected Certificate of Authority.

Current Findings: The Company has a Certificate of Authority which authorized the Company to write wind, fire and liability lines of business.

Conflict of Interest

Comment: It was recommended the employees of FMFIC who are also agents of Phillip W. Spencer Agency sign conflict of interest disclosure forms.

Company Response: All employees currently sign conflict of interest forms.

Current Findings: The Company currently requires all employees, directors and officers to sign conflict of interest disclosure forms.

Insurance Products and Related Practices

Comment: It was recommended that the Company's contract with Phillip W. Spencer Agency, as well as the Company's contracts with its agents, be amended to contain provisions designating responsibility for obtaining errors and omissions insurance, the timely delivery of an application to the home office, and that the application should be fully completed before it is delivered to the home office.

Company Response: The Company amended the contract with the Phillip W. Spencer Agency to require the agency to provide errors and omissions coverage on the agents. The Company Policies and Procedures Manual requires applications to be delivered to the home office timely and fully completed.

Current Findings: The Company's agent agreement requires the agency to provide errors and omissions insurance for the agents, and the Company's Policies and Procedures Manual provides for timely delivery of fully completed applications to the home office.

HISTORY

General

The Company was originally organized on August 5, 1895, and incorporated on October 10, 1895, as Farmers Mutual Fire Insurance Company of Chariton County. On March 30, 2000, the Company changed its name to Chariton County Mutual Insurance Company. The Company operates under Sections 380.201 through 380.611 RSMo (Extended Missouri Mutual Companies).

Management

In accordance with the Articles of Incorporation, the annual meeting of the Company's members is held on the last Thursday in March, at the home office of the Company or at such other place as may be designated by the Board of Directors. Special meetings of the members may be called by the Board of Directors at any time and shall be called upon petition of one-fourth of the members. Eight members shall constitute a quorum at any membership meeting. Proxy voting is not permitted.

The management of the Company is vested in the Board of Directors, who are elected from the general membership. The Board of Directors consists of nine members, serving staggered, three-year terms. All directors must be policyholders of the Company. The Board of Directors meets approximately every other month, and the directors are compensated \$100 per meeting attended.

Members serving on the Board of Directors as of December 31, 2003, were as follows:

| <u>Name and Address</u> | <u>Occupation</u> | <u>Term</u> |
|--|--------------------------|-------------|
| Eugene Abeln Route 2 Box 48 Salisbury, Missouri | Farmer | 2002-2005 |
| John Summers Route 1 Box 5 Triplett, Missouri | Farmer | 2002-2005 |
| Hubert Gladbach Route 1 Box 61 Mendon, Missouri | Farmer | 2001-2004 |
| Richard Miller Route 1 Box 67 Keytesville, Missouri | Business Owner | 2003-2006 |
| Ronnie McGilvray Route 1 Box 220 Mendon, Missouri | Farmer | 2001-2004 |
| L.E. Manson Route 1 Box 62 Dalton, Missouri | Farmer | 2001-2004 |
| George A. Schupback Route 2 Kirksville, Missouri | Farmer | 2003-2006 |
| Vernon E. Vaughn Route 2 Box 139 Marceline, Missouri | Farmer/Railroad Employee | 2003-2006 |
| Floyd Rodgers Route 1 Box 86 New Cambria, Missouri | Retired | 2002-2005 |

The Board of Directors elects for a term of one year a President, Vice-President, and Secretary, who may also serve as Treasurer when so designated by the Board.

The officers of the Company serving at December 31, 2003, were as follows:

| | |
|------------------|---------------------|
| L.E. Manson | President |
| Ronnie McGilvray | Vice-President |
| Phillip Spencer | Secretary/Treasurer |

Conflict of Interest

The Company has written conflict of interest procedures for the disclosure of material conflicts of interest or affiliations by its directors and officers. The Company has its directors and officers sign conflict of interest statements on an annual basis, and no material potential conflicts were disclosed.

Corporate Records

A review was made of the Articles of Incorporation (Articles) and the Bylaws of the Company. Both the Articles and Bylaws were amended during the examination period.

On March 30, 2000, the Articles were amended to change the Company's name from "Farmers Mutual Fire Insurance Company of Chariton County" to "Chariton County Mutual Insurance Company." On March 27, 2003, the Articles and Bylaws were amended, changing all references from "assessment" to "premium," to facilitate the Company's conversion from an assessable to a non-assessable mutual.

The minutes of the membership and the Board of Directors' meetings were reviewed for the period under examination. In addition, the Company's policies for investments and underwriting were reviewed. The minutes and records of the Company appear to properly reflect corporate transactions and events.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a fidelity bond providing a limit of liability of \$100,000. The fidelity bond coverage of the Company meets the minimum amount suggested in the guidelines promulgated by the NAIC, which is between \$50,000 and \$75,000 in coverage.

The Company carries directors' and officers' liability coverage with per claim and aggregate limits of \$2,000,000 and a \$500 deductible for each director and officer each loss and a \$2,500 deductible in aggregate as it pertains to directors and officers liability.

The Company's in-house agency purchases errors and omissions insurance for its agents with an aggregate limit of \$1,000,000 and a \$1,000 deductible.

The Company has business owner's coverage on its buildings and contents. The policy provides coverage of \$45,314 on the building and \$10,000 on office contents. The policy also provides for business liability coverage with an aggregate limit of \$500,000 and medical expense limits of \$5,000 per person.

The insurance coverage appears adequate.

EMPLOYEE BENEFITS

The Company has three full-time employees. The Company provides paid vacation and sick leave for the employees. The Company makes an annual contribution to each employee's individual retirement account. The employees also participate in a profit sharing plan under which an amount, approved annually by the Board, is split equally among the employees if certain financial and growth objectives are met. It appears the Company has made adequate provisions in its financial statements for the employee benefit obligations.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

The Company is licensed by the Missouri Department of Insurance as an Extended Missouri Mutual Company operating under Sections 380.201 through 380.611 RSMo. (Extended Missouri Mutual Companies). The Company is authorized to write fire, wind and liability insurance in all counties in the State of Missouri. The Company writes fire, wind and liability coverage.

The Company's policies are sold by three agents that are members of the in-house agency, Phillip W. Spencer Insurance Agency. The agency and agents do not receive commissions from the Company. The agents are employees of the Company, and are compensated by the Company in the form of set hourly or monthly wages.

Policy Forms and Underwriting Practices

The Company uses AAIS policy forms provided by the Missouri Association of Mutual Insurance Companies. The policies are continuous. Property inspections and adjusting functions are performed by the agents. Rates are determined by the Board of Directors. Renewal billings are mailed directly to the insured.

GROWTH AND LOSS EXPERIENCE OF THE COMPANY

| | Admitted Assets | Liabilities | Gross Assessment | Gross Losses | Investment Income | Underwriting Income | Net Income |
|------|--------------------|-------------|---------------------|-----------------|----------------------|------------------------|------------|
| 2003 | \$2,379,562 | \$345,594 | \$712,539 | \$364,960 | \$39,886 | \$33,187 | \$68,829 |
| 2002 | 2,281,398 | 316,258 | 640,839 | 266,772 | 58,271 | 166,782 | 215,858 |
| 2001 | 2,116,436 | 367,182 | 627,346 | 324,631 | 95,520 | 78,681 | 158,389 |
| 2000 | 1,758,951 | 11,161 | 626,283 | 386,795 | 83,154 | 31,504 | 100,756 |
| 1999 | 1,643,457 | 12,997 | 72,383 | 212,998 | 72,384 | 28,369 | 109,671 |

At year-end 2003, 1,185 policies were in force.

REINSURANCE

General

The Company's reinsurance premium activity on a direct-written, assumed and ceded basis for the period under examination is shown below:

| | <u>1999</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> | <u>2003</u> |
|---------|------------------|------------------|-----------------|-----------------|-----------------|
| Direct | \$580,172 | \$626,283 | \$627,346 | \$640,839 | \$712,539 |
| Assumed | 0 | 0 | 0 | 0 | 0 |
| Ceded | <u>(243,305)</u> | <u>(277,501)</u> | <u>(78,910)</u> | <u>(88,007)</u> | <u>(93,057)</u> |
| Net | \$336,867 | \$348,782 | \$548,436 | \$552,832 | \$619,482 |

Assumed

The Company does not reinsure other companies.

Ceded

The Company has all of its reinsurance through Grinnell Mutual Reinsurance Company (the

reinsurer) under a single reinsurance contract for fire, wind and liability risks. The aggregate excess section of the agreement covers fire and wind risks. The Company's annual aggregate net retention, or attachment point, is based upon the Company's ten-year average fire loss ratio plus a load, which is mutually agreed upon. The reinsurer is liable for 100% of losses in excess of this retention. The attachment point for 2003 was \$351,625 and the annual premium paid was \$.2880 per \$1,000 of adjusted gross fire risks in force.

The agreement also provides for liability risk coverage. The Company cedes 100% of the risk and premium to the reinsurer and receives a 20% ceding commission.

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that any assuming reinsurer should fail to perform its obligations under its reinsurance agreement with the Company.

ACCOUNTS AND RECORDS

The accounting records are maintained by the Company on an accrual basis. The Company's accountant, Harden, Cummins, Moss & Miller, LLC, performs an annual audit of the Company's financial statements, and prepares the Company's Annual Statement and federal income tax return.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2003, and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the Annual Statement and/or comments regarding such are made in the "Notes to the Financial Statements," which follow the Financial Statements. (The failure of any column of numbers to add to its respective total is due to rounding or truncation.)

There may have been differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial, concerning their

effect on the financial statements. Therefore, they were communicated to the Company and noted in the workpapers for each individual annual statement item.

ANALYSIS OF ASSETS
December 31, 2003

| | |
|--------------------------------|-------------|
| Real Estate | 19,000 |
| Cash on Deposit | 2,336,691 |
| Premium Receivable | 6,909 |
| Reinsurance Recoverable | 2,915 |
| Federal Income Tax Recoverable | 4,581 |
| Interest Due and Accrued | 6,647 |
| Asset Write-Ins | 2,819 |
| | ----- |
| Total Assets | \$2,379,562 |
| | ===== |

LIABILITIES, SURPLUS AND OTHER FUNDS
December 31, 2003

| | |
|-------------------------------|--------------|
| Losses Unpaid | \$ 28,919 |
| Ceded Reinsurance Payable | 8,204 |
| Unearned Premium | 300,216 |
| Liability Write-Ins | 8,255 |
| | ----- |
| Total Liabilities | \$ 345,594 |
| | ----- |
| Guaranty Fund | \$ 150,000 |
| Other Surplus | 1,883,968 |
| | ----- |
| Total Surplus | \$ 2,033,968 |
| | ----- |
| Total Liabilities and Surplus | \$ 2,379,562 |
| | ===== |

STATEMENT OF INCOME
December 31, 2003

| | |
|--------------------------------|------------|
| Net Premium | \$ 673,886 |
| Net Losses Incurred | (355,874) |
| Other Underwriting Expenses | (284,825) |
| | ----- |
| Net Underwriting Income (Loss) | \$ 33,187 |
| | ----- |
| Investment Income | \$ 39,886 |
| Other Income | 2,495 |
| | ----- |
| Gross Income | \$ 75,568 |
| Federal Income Tax | (6,739) |
| | ----- |
| Net Income (Loss) | \$ 68,829 |
| | ===== |

CAPITAL AND SURPLUS ACCOUNT
December 31, 2003

| | |
|---|--------------|
| Policyholders' Surplus, December 31, 2002 | \$ 1,965,140 |
| Net Income (Loss) | 68,829 |
| | ----- |
| Policyholders' Surplus, December 31, 2003 | \$ 2,033,968 |
| | ===== |

NOTES TO THE FINANCIAL STATEMENTS

There were no notes to the financial statements.

EXAMINATION CHANGES

There were no examination changes.

GENERAL COMMENTS AND RECOMMENDATIONS

None.

SUBSEQUENT EVENTS

None.

ACKNOWLEDGMENT

The assistance and cooperation extended by the employees of Chariton County Mutual Insurance Company during the course of this examination is hereby acknowledged and appreciated.

VERIFICATION

State of Missouri)
) ss
County of Cole)

I, Shannon W. Schmoeger on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only the facts appearing upon the books, records or other documents of the company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

Shannon W. Schmoeger, CFE
Financial Examiner
Missouri Department of Insurance

Sworn to and subscribed before me this _____ day of _____, 2004.

My commission expires:

Notary Public

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

Frederick G. Heese, CFE, CPA
Audit Manager – Kansas City
Missouri Department of Insurance